

**OFFICE OF THE MINISTER OF COMMERCE
OFFICE OF THE MINISTER OF CONSUMER AFFAIRS**

The Chair
CABINET ECONOMIC DEVELOPMENT COMMITTEE

**REVIEW OF FINANCIAL PRODUCTS AND PROVIDERS: CONSUMER DISPUTE
RESOLUTION AND REDRESS**

PROPOSAL

- 1 This paper seeks the Committee's agreement to the establishment of a comprehensive, industry-based consumer dispute resolution system to improve consumer access to redress in the financial sector.
- 2 This paper forms part of a suite of papers relating to the Reviews of Financial Products and Providers and Financial Advisers.

EXECUTIVE SUMMARY

- 3 Effective dispute resolution and redress mechanisms are essential to encouraging consumers to participate in financial markets and promoting market discipline for financial providers.
- 4 A discussion paper, released in August 2006, put forward a number of options for improving consumer access to dispute resolution and redress. These options included improved consumer education, enhanced civil remedies and specialist courts/tribunals, and voluntary and/or mandatory industry-based dispute resolution schemes.
- 5 Submissions on the discussion paper supported the view that there is sufficient evidence of a problem to warrant further government action to improve access to redress in order to promote consumer confidence in financial markets.
- 6 This paper proposes the establishment of a comprehensive, industry-based dispute resolution system across the financial sector. The key features of the proposed system include:
 - a Membership of an approved dispute resolution scheme will be mandatory for financial providers who are required to be registered and who transact with consumers. Membership of an approved dispute resolution scheme will also be mandatory for financial advisers who deal with members of the public. The legislation proposed in the paper "Review of Financial Products and Providers: Registration of Financial Service Providers" will establish rules for which financial providers must belong to a dispute resolution scheme and which consumers may have access to dispute

resolution by reference to the definitions and applicability of other legislation governing specific sectors of the financial industry.

- b An approved dispute resolution scheme is one that has satisfied the Minister of Commerce that it meets criteria of accessibility, independence, fairness, accountability, efficiency and effectiveness. In deciding whether to approve a scheme, the Minister must give regard to some mandatory considerations relating to the governance of the scheme, periodic reviews, the scheme's funding, the cost to consumers, membership restrictions, the scheme's jurisdiction, limits on liability of scheme members, evidence and processes, awareness, promotion and education, and reporting to stakeholders.
 - c It is anticipated that more than one scheme will be approved, and financial providers will have freedom to choose which scheme they wish to join.
 - d In the event of no schemes meeting the approval criteria or if there is not full coverage of the financial industry by those schemes which are approved, reserve powers will allow for a government-established scheme.
 - e A decision of a scheme will be binding on the member in relation to whom it is made, but will not preclude a consumer from rejecting the scheme's decision and taking alternative court action against a financial provider.
 - f The dispute resolution system will be fully funded by industry.
 - g Government involvement will be limited to approving schemes (including periodic renewal), receiving periodic reports, and powers of inspection if necessary, rather than involvement in the day-to-day operation of a scheme. Re-approval is to be obtained by schemes at 10 year intervals. Periodic reporting is to be annual and set out basic information about the activities of the scheme (eg number and type of complaints considered, promotional activities undertaken, etc), as well as identifying any systemic issues which the scheme considers require attention by government.
- 7 In addition to access to redress, improved consumer financial capability is also vital in promoting consumer confidence in financial markets. The Ministry of Economic Development and other relevant agencies are working on various initiatives to improve consumer financial capability.

BACKGROUND

- 8 A Review of Financial Products and Providers commenced in 2005. Its key objective is to develop an effective and consistent framework for the regulation of non-bank financial institutions and financial products with the aim of promoting confidence and participation in the financial markets by investors and institutions, and achieving a sound and efficient non-bank financial sector.

- 9 On 23 August 2006, the Cabinet Economic Development Committee [EDC Min (06) 13/7 refers] agreed to the release of a discussion paper setting out options for improving consumer access to dispute resolution and redress.

Problem definition

- 10 The majority of submissions on the August 2006 discussion paper identified problems in relation to consumer confidence and access to redress mechanisms, although some submissions strongly argued that there were no current problems. On balance, I believe that there is sufficient evidence of a problem to warrant further government action to improve access to redress in order to promote consumer confidence in financial markets.
- 11 The discussion paper also noted recent consumer surveys which showed that, while the level of consumer problems with misleading or unfair treatment by financial providers is relatively low, there are significant problems with consumers seeking redress. Common reasons given by consumers included “did not know who to complain to”, “did not think it would make a difference”, and “couldn’t be bothered”. These responses indicated problems for consumers in relation to both knowing where to go to seek redress, and in having the capability to effectively use existing dispute resolution and redress mechanisms.
- 12 Dispute resolution and redress, which aims to provide a forum for consumers to have an independent person to listen to their concerns and potentially order compensation where the consumer has suffered a loss as a result of illegal or inappropriate conduct by a financial provider, should be contrasted with discipline and regulatory oversight, which is concerned with overall market stability, rather than the effects on any individual consumer.
- 13 While other proposals arising from the reviews of financial products and providers and financial advisers will help reduce the incidence of consumer problems, they will not completely eliminate the need for consumers to be able to access mechanisms to resolve disputes and seek redress if the provider fails to meet the consumer’s reasonable expectations.

Need for government action

- 14 Effective dispute resolution and redress mechanisms are essential to encouraging consumers to participate in financial markets and promoting market discipline for financial providers.
- 15 Existing voluntary industry-based dispute resolution schemes, such as the Banking Ombudsman and Insurance & Savings Ombudsman, provide effective access to redress for consumers. These two schemes cover a large proportion of the financial sector; however, they do not currently extend to building societies, credit unions, finance companies, financial advisers and some superannuation schemes.
- 16 It is unlikely that these sectors will develop voluntary dispute resolution schemes. Therefore, further government action is needed to improve access to redress in order to promote consumer confidence in financial markets.

OPTIONS

- 17 The discussion paper proposed several options to improve consumer dispute resolution and redress.
- a Status quo (voluntary, sector-specific dispute resolution).
 - b Improved consumer education and information to build capability of consumers to make informed choices so that they will avoid unsuitable products.
 - c Enhanced civil remedies and specialist courts/tribunals, for example a specialist Disputes Tribunal for financial disputes.
 - d Mandatory industry-based dispute resolution, with multiple schemes.
 - e A single mandatory industry-based dispute resolution scheme.

Views expressed by submitters

- 18 Submissions on the discussion paper did not generate a clear consensus on a preferred option. Submissions were generally in favour of a mandatory industry-based dispute resolution system, however, there were also arguments in favour of a voluntary dispute resolution system (status quo), and use of the courts as the appropriate place to resolve disputes.
- 19 Those submissions which favoured mandatory industry-based dispute resolution were fairly evenly split between the single scheme and multiple schemes approaches, with a slight majority in favour of multiple schemes.

Preferred option

- 20 I recommend adopting for mandatory industry-based dispute resolution, and allowing for the establishment of multiple schemes. Submissions were not able to mount a convincing argument that the efficiency and economies of scale of a single scheme would be sufficient to outweigh the flexibility and greater industry commitment of a multiple schemes approach.
- 21 It would be counter-productive to tamper with existing schemes that are operating efficiently for the sake of creating a unified, cross-industry scheme. As each sector of the financial industry is quite distinct in terms of the products they provide, participants in each sector should be free to choose the form of dispute resolution that best suits the particular characteristics of the sector, whether that be a sector-specific dispute resolution scheme or a wider scheme.
- 22 The industry-based dispute resolution system is intended to operate as a complement to the courts. This means that consumers will still retain their right to take court action if they wish.

KEY ISSUES

Mandatory participation by financial providers

- 23 In order to provide effective coverage of the financial sector, I propose that membership¹ of an approved dispute resolution scheme be mandatory for financial providers who are required to be registered and who transact with consumers.
- 24 The accompanying paper entitled “Review of Financial Products and Providers: Registration of Financial Service Providers” sets out the categories of entities which will be required to be registered. They are:
- banks;
 - friendly societies;
 - credit unions;
 - building societies;
 - industrial and provident societies;
 - finance companies;
 - issuers of equity and debt securities;
 - issuers of collective investment schemes;
 - trustees supervising these issuers;
 - insurers;
 - platform and portfolio service providers and custodians.
 - lending businesses;
 - financial leasing businesses;
 - money or value transfer services (eg money remittance);
 - money and currency changers.
- 25 I also propose that the dispute resolution system will also apply to financial advisers covered by the accompanying paper entitled “Financial Advisers – A new regulatory framework”.

¹ The term “membership” in this paper does not prescribe any particular relationship between the financial service provider and the dispute resolution scheme. For example, the “membership” requirement could be satisfied through a shareholding in the dispute resolution scheme, or through a contractual or service-based relationship. Note however that the dispute resolution scheme must satisfy the approval criteria, including governance requirements.

- 26 The registration requirements are aimed at establishing a comprehensive supervisory framework for financial service providers. On the other hand, the dispute resolution system is aimed at promoting consumer confidence in the financial system. Therefore, it is not necessary for all financial service providers to belong to a dispute resolution scheme, but only those financial service providers which transact with “consumers”.
- 27 The definition of consumer may be different depending on the particular sector, and will need to be consistent with the other definitions of consumer that flow from the consumer protection and other regulatory requirements in that sector. For example, in the area of securities, the Securities Act provides consumer protection (through disclosure requirements) for “members of the public”. Under the proposal in this paper, the requirement for a financial provider offering securities to belong to a dispute resolution scheme would be referenced to the Securities Act, ie those issuers who offer securities to a member of the public must belong to an approved dispute resolution scheme. Likewise, this would also set out which “consumers” may access the dispute resolution system; in this case, it is “members of the public” as defined under the Securities Act.
- 28 As another example, in the area of credit, the Credit Contracts and Consumer Finance Act applies to “consumer credit contracts”, that is, where the debtor is a natural person and enters into the contract primarily for personal, domestic or household purposes. Under the proposal in this paper, the requirement for credit providers to belong to a dispute resolution scheme would be referenced to the Credit Contracts and Consumer Finance Act, ie those creditors who provide consumer credit contracts must belong to an approved dispute resolution scheme.
- 29 In other sectors, for example non-bank deposit takers or financial advisers, it may be appropriate to recognise that information and power imbalances apply to small businesses, as well as consumers. In these sectors therefore, it may be appropriate to allow small businesses access to dispute resolution.
- 30 I have asked the Ministry of Economic Development to give further consideration to the detailed definitions that will be required and I will report back to EDC by 31 August 2007.
- 31 However other financial providers may also voluntarily choose to join a scheme. Similarly, a scheme may provide in its rules that other persons are entitled to have a complaint heard by the scheme.

Approval of dispute resolution schemes

Why approve schemes

- 32 In order to ensure that dispute resolution schemes promote consumer confidence, it will be necessary to have a mechanism to ensure that schemes meet appropriate standards. Most submissions considered that there will be a need for a process for approval of dispute resolution schemes by government, however, some submissions said that oversight by an independent body (such as the current

independent commissioners overseeing the Banking Ombudsman and Insurance & Savings Ombudsman) is appropriate.

Who will approve schemes

- 33 Those submissions which supported approval by government were split on whether approval should be by the Minister of Commerce or by a regulatory body such as the Securities Commission. As there will be a split in regulatory responsibility across the financial industry (ie Securities Commission and Reserve Bank will each have specific areas of oversight), I propose that responsibility for approving dispute resolution schemes lie with a Minister. In addition, the regulators' focus is on the financial system as a whole, rather than individual consumers.
- 34 Dispute resolution relates to financial markets, therefore, it is within the responsibility of the Minister of Commerce. However, taking into account the importance of financial markets to economic policy, and the particular role of consumer protection, I propose that legislation provide for the approval of dispute resolution schemes by the Minister of Commerce in consultation with the Minister of Consumer Affairs and Minister of Finance.
- 35 The legislation will provide for appropriate checks and balances in the approval process, including a requirement for the Minister to be satisfied that the scheme has undertaken appropriate consultation, timeframe for decisions, method of notifying approval, and other matters.

Approval criteria

- 36 Recognising that what is appropriate for one sector of the financial industry may not be appropriate for another, there will need to be flexibility in the criteria for approval of a scheme. I propose that legislation set out broad principle-based approval criteria of accessibility, independence, fairness, accountability, efficiency, and effectiveness.
- 37 In addition to the principle-based approval criteria, the legislation will establish some mandatory considerations that the Minister must have regard to in deciding whether to approve a scheme.
- 38 To assist affected parties in complying with the new regime, the Ministry of Economic Development will produce educational material for dispute resolution schemes to help them meet their obligations in order to obtain approval, and for financial providers, to inform them of their obligation to join a dispute resolution scheme.
- 39 It is proposed that legislation provide that the Minister may give his or her approval subject to conditions and/or may impose conditions on a scheme, or revoke the approval of a scheme, if the scheme experiences any major changes after approval, such as admission of new members from a different sector, changes in directors or senior management, or changes to the scheme's rules or terms of reference. Conditions might cover issues such as the type of cases or

sectors where a scheme may operate, requirements for training, governance requirements, internal review, etc.

- 40 The proposal will have fiscal implications for the Ministry of Economic Development in order to provide advice regarding applications for approval. The fiscal implications of the proposals are discussed in the accompanying paper “Reviews of Financial Products and Providers and Financial Advisers – Overview Paper”.

Mandatory considerations

- 41 The following paragraphs outline the mandatory considerations I propose that the Minister must have regard to in deciding whether to approve a scheme.

Governance of schemes

- 42 Schemes will have broad flexibility to develop their own governance arrangements. The Minister must have regard to the extent to which the scheme’s governance arrangements ensure the independence and accountability of the scheme. For example, this will require a balance of industry and consumer representatives on the governing board.
- 43 The Minister must also have regard to the competency of the directors and senior management of the scheme. This could be achieved by “negative assurances”, for example, a scheme certifying in its application for approval that its directors and senior managers have no criminal convictions, have not been bankrupt, disqualified as directors, etc.

Periodic reviews

- 44 Periodic review is an important element in ensuring that a scheme continues to fulfil its role. As discussed in paragraph 62 below, a scheme must undertake a review and seek renewal of its approval at 10 year intervals. In addition to this re-approval requirement, more frequent reviews will also be useful for schemes, particularly schemes which are newly established or which have taken on new members. These reviews could be internal reviews (ie conducted by the scheme itself) or an independent review by an outside reviewer. In deciding whether to approve a scheme, the Minister must have regard to whether the scheme’s rules provide for periodic reviews of the scheme, and what type of reviews are required.

Funding of schemes

- 45 It is expected that the dispute resolution system will be fully funded by industry. In deciding whether to approve a scheme, the Minister must have regard to whether the scheme has adopted procedures to ensure that it has adequate funding to enable it to operate effectively.

Cost to consumers

- 46 The dispute resolution system is intended to be a low-cost complement to the court system. Therefore, access to the dispute resolution scheme is intended be

free or low-cost for consumers, for example no more than the equivalent cost to lodge a claim in the Disputes Tribunal. In deciding whether to approve a scheme, the Minister must have regard to the cost to consumers to lodge a complaint with the scheme.

Membership restrictions

- 47 It will be important to ensure that all members of a scheme are committed to the success of the scheme. The Minister must have regard to the extent to which a scheme's members cover a particular sector or sectors, however, each scheme will be free to set restrictions or qualifications on membership of the scheme to ensure that the scheme operates in an efficient and effective way.

Jurisdiction of schemes

- 48 There are three broad types of likely complaints, which arise out of obligations with different legal force (1) complaints that could be the subject of litigation (eg breach of contract or statutory obligation); (2) complaints of general unfairness (eg maladministration); (3) complaints about breach of an industry code of practice.
- 49 In deciding whether to approve a scheme, the Minister must have regard to whether the scheme has adopted a minimum jurisdiction covering breach of contract or statutory obligation, and breach of an industry code, as this reflects the jurisdiction available to consumers through the courts. Schemes will also be free to adopt a wider jurisdiction, covering complaints of general unfairness, if the scheme members so desire.
- 50 Recognising that in most cases where a large amount is at issue the participants are able to access legal advice, a scheme may provide in its rules for a monetary limit on the complaints it is empowered to consider. A monetary limit may also be important in order to limit the maximum potential exposure of a financial provider. As the appropriate amount for a monetary limit will depend on the particular sector, and will inevitably need to change over time, it is not appropriate to provide for this in legislation. I propose that it form part of the approval criteria, that is, in deciding whether to approve a scheme, the Minister must have regard to whether a proposed monetary limit is appropriate for the particular sector or type of business carried on by scheme members.

Evidence and processes

- 51 In order to provide a simpler and cheaper alternative to the courts, a scheme should adopt rules which provide for simplified processes for the resolution of disputes. In deciding whether to approve a scheme, the Minister must have regard to whether the scheme's rules provide that it is free to consider any information or make any enquiry as it sees fit and can have reference to what the scheme considers fair and reasonable in the circumstances, rather than strict adherence to legal rules.

Awareness, promotion and education

- 52 A scheme should take steps to promote awareness of itself amongst consumers. This means that the scheme should promote itself, and should also require member firms to inform their customers of the existence of the scheme. In deciding whether to approve a scheme, the Minister must have regard to the scheme's obligations under its rules to engage in awareness, promotion and education.²

Reporting to stakeholders

- 53 It is important that schemes report regularly to their members, the public and other stakeholders. This will help promote confidence in the scheme. In deciding whether to approve a scheme, the Minister must have regard to the scheme's obligations under its rules to report to stakeholders.

Reserve powers to establish a scheme by regulation

- 54 Given that membership of an approved scheme is to be a mandatory requirement for financial providers under the proposed new regime, I anticipate that one or more existing dispute resolution schemes will seek approval under the new regime. In addition, I anticipate that those sectors which are not currently covered by a voluntary scheme will also seek approval for a scheme or schemes. Officials have had discussions with the existing voluntary schemes (Banking Ombudsman and Insurance & Savings Ombudsman), which have both indicated that they are likely to seek approval under the proposed regime. Officials have also had discussions with those bodies which are likely to seek approval as an Approved Professional Body under the financial advisers regime, and those bodies have indicated that they will participate actively in the proposed dispute resolution system.
- 55 However, I propose that the legislation allow for reserve powers under which the Minister may, by regulation, establish a dispute resolution scheme (the "reserve scheme"). The reserve powers will be able to be exercised if there are no approved schemes, or if there is not full coverage of the financial industry by those schemes which are approved. I expect that any gaps in coverage would become apparent through discussion with industry during the transition period for implementation of the new legislation. This would allow sufficient time for establishment of a reserve scheme, if necessary.
- 56 The reserve scheme would be subject to the same regulatory requirements as an industry-based scheme and would be required to meet the principles of accessibility, independence, fairness, accountability, efficiency, and effectiveness. Financial providers would be able to satisfy their mandatory membership obligation by joining either the reserve scheme or an approved scheme.

² Note that requirements for firms to inform consumers about the scheme may also be covered by the regulation of disclosure in specific sectors. For example, the proposed regime for financial advisers will require a financial adviser to disclose which dispute resolution scheme they are a member of.

- 57 The reserve powers will also permit a levy to be imposed on members of the reserve scheme to fund the establishment and operation of the reserve scheme.
- 58 This paper seeks Cabinet's in principle agreement to legislation providing for a reserve scheme, similar to the powers contained in the amendments to the Telecommunications Act. I will report back to Cabinet by 31 July 2007 with a more detailed proposal covering the powers of the reserve scheme, calculation of the levy and the process for establishment of the reserve scheme.

Binding decisions and appeals

- 59 To alleviate negative consumer perceptions about an industry-based scheme, consumers should have an opportunity to take alternative action through the court system if unsatisfied with the decision of the scheme. The scheme's rules must provide, subject to a limited exception, that a decision of the scheme is binding on the member in relation to whom it is made, but do not preclude a consumer from rejecting the scheme's decision and taking alternative court action against a financial provider. As discussed in paragraph 50 above, in order to limit the maximum potential exposure of a financial provider, a scheme may choose to impose a monetary limit on claims.
- 60 A member's limited right to appeal from a decision of a scheme will be similar to rights available under the Disputes Tribunal Act for appeals against an order of a Disputes Tribunal. That is, an appeal is only allowed on the grounds that the proceedings were carried out in an unfair manner.

Funding of the dispute resolution system

- 61 It is expected that the dispute resolution system will be fully funded by industry. However, there will be fiscal implications for the Ministry of Economic Development in providing guidance and working with schemes prior to approval, possibly including a need for seed funding for the establishment of some schemes until they are in a position to accept members. The fiscal implications of the proposals are discussed in the accompanying paper "Reviews of Financial Products and Providers and Financial Advisers – Overview Paper".

Monitoring and supervision

- 62 It is proposed that government involvement will be limited to approving schemes (including periodic renewal), receiving periodic reports, and powers of inspection if necessary. There will be no government involvement in the day-to-day operation of a scheme. A scheme must undertake a review and seek renewal of its approval at 10 year intervals. The review and renewal will involve a full re-assessment of the scheme against the approval criteria, and will also take into account previous reporting by the scheme. If a scheme fails to obtain re-approval, a grace period will be available for members to join a new scheme.
- 63 Regulations will set out the frequency and content of reporting. I propose that the regulations require an annual report to the approving Minister, setting out basic information about the activities of the scheme (eg number and type of complaints considered, promotional activities undertaken, etc), as well as

identifying any issues which may have a wider impact on the financial sector and which the scheme considers require regulatory review by government. I propose also that the Minister be empowered to seek further explanations from a scheme regarding the matters included in an annual report.

- 64 There will also be an obligation for schemes to maintain a list of members and to immediately notify the Registrar of Financial Service Providers³ if a member is expelled from the scheme.
- 65 The Retirement Commissioner is empowered under section 83(e) of the New Zealand Superannuation and Retirement Income Act 2001 to monitor the effectiveness of persons who have been appointed (other than under statutory authority) to consider complaints and disputes about savings and investments and, if appropriate, to make recommendations to any person. It is proposed that the Retirement Commissioner retain this function.
- 66 Although the Retirement Commissioner's monitoring role will be independent from the supervision of approved schemes through their annual reports and the 10 year renewal, it is expected that any findings or recommendations made by the Retirement Commissioner will be useful in informing the Minister's decision on whether to renew a scheme's approval.

Relationships between multiple schemes

- 67 While there may be some overlap if a complaint involves firms who are members of different schemes, it is expected that schemes will develop procedures to cooperate with each other, for example by coordinating cases and learning from each other.
- 68 It is in each scheme's own interests to operate efficiently. Therefore, I anticipate that schemes will, if it is appropriate, voluntarily cooperate to share resources and/or establish a single entry point (eg a shared call centre and/or website) for consumers to access the various schemes. Therefore, it is not necessary to impose a regulatory requirement on approved schemes to cooperate with each other.

CONSUMER FINANCIAL CAPABILITY

- 69 Most submissions argued that improved consumer financial capability is needed, but that it is not a solution in its own right. Submissions identified two types of consumer education (1) to enable consumers to make better decisions when entering into transactions, (2) to inform consumers about the availability of dispute resolution and redress mechanisms. Other elements of the Review of Financial Products and Providers will address particular consumer financial capability issues. For example, the work on security offerings and collective investment schemes will provide an enhanced disclosure regime to help consumers better understand the products they are purchasing.

³ Refer to the accompanying paper "Review of Financial Products and Providers: Registration of Financial Service Providers" for further details about the proposed Registrar of Financial Service Providers.

- 70 The Ministry of Economic Development and other relevant agencies are working on various initiatives to improve consumer financial capability, however, that work will be addressed outside the proposals contained in this paper or the Review of Financial Products and Providers.

CONSULTATION

- 71 Government agencies consulted are listed in the accompanying paper “Reviews of Financial Products and Providers and Financial Advisers - Overview Paper”.
- 72 The proposals were the subject of a discussion paper which was released in August 2006, along with other discussion papers in the Review of Financial Products and Providers. 139 submissions were received on the RFPP papers, of which 42 contained comments on consumer dispute resolution.

FISCAL IMPLICATIONS

- 73 The proposals in this paper will result in additional roles and functions for the Ministry of Economic Development. The fiscal implications of the proposals are discussed in the accompanying paper “Reviews of Financial Products and Providers and Financial Advisers – Overview Paper”.

HUMAN RIGHTS

- 74 Overall the proposals in the Cabinet paper do not appear to be inconsistent with the New Zealand Bill of Rights Act 1990, or the Human Rights Act 1993. However, if any issues do arise officials from the Ministry of Economic Development and Ministry of Justice will work together to ensure that the legislation is consistent with the Bill of Rights Act. A final view as to whether the proposals will be consistent with the Bill of Rights Act will be possible once the legislation has been drafted.

LEGISLATIVE IMPLICATIONS

- 75 New legislation is required to implement the proposals in this paper. A Financial Service Providers Registration and Dispute Resolution Bill, to be passed in 2008, will contain these proposals (refer to Overview paper).

REGULATORY IMPACT ANALYSIS

- 76 The Ministry of Economic Development (MED) confirms that the Code of Good Regulatory Practice and the regulatory impact analysis requirements, including the consultation RIA requirements, have been complied with. A RIS was prepared and the Regulatory Impact Analysis Unit considers the RIS and the RIA analysis undertaken to be adequate. A draft RIS was circulated with the Cabinet paper for departmental consultation purposes.

PUBLICITY

- 77 Once Cabinet has reached a decision on this paper and the other accompanying papers on the Review of Financial Products and Providers, I will release a press statement to signal to the public the Government's policy decisions in this area.

Targeted consultation will then be undertaken on an exposure draft of the Bill later this year so that members of the public with expertise in the financial sector area will have a chance to comment on the proposals at a more detailed level.

RECOMMENDATIONS

- 78 It is recommended that the Committee
- 1 **Note** that on 23 August 2006, the Cabinet Economic Development Committee invited the Minister of Commerce to submit a further paper to EDC by April 2007 seeking approval for policy decisions on the Review of Financial Products and Providers.
 - 2 **Note** that this paper is part of a suite of Cabinet papers relating to the Reviews of Financial Products and Providers and Financial Advisers.
 - 3 **Agree** to an industry-based consumer dispute resolution system with the following key features:
 - 3.1 Dispute resolution schemes must be approved by the Minister of Commerce; and
 - 3.2 Membership of an approved dispute resolution scheme will be mandatory for all (as specified in the accompanying paper Registration of Financial Service Providers):
 - (a) financial institutions that are required to be registered; and
 - (b) financial advisers;

who provide products or services to consumers; and
 - 3.2.1 **Invite** the Minister of Commerce to report back to EDC by 31 August 2007 on how consumers will be defined; and
 - 3.3 The purpose of the dispute resolution system is to provide a simple, low-cost avenue for consumers to seek redress; and
 - 3.4 The dispute resolution system will be fully funded by industry.
 - 4 **Agree** that the Minister of Commerce may, following consultation with the Minister of Consumer Affairs and Minister of Finance, approve a dispute resolution scheme if the scheme meets criteria of accessibility, independence, fairness, accountability, efficiency and effectiveness, and if the scheme meets minimum standards set out in legislation.
 - 5 **Agree** that the scheme approval process include appropriate checks and balances, including a requirement for the Minister of Commerce to be satisfied that the scheme has undertaken appropriate consultation, timeframe for decisions, method of notifying approval, and other matters.

- 6 **Agree** that the Minister may impose conditions on the approval of a scheme or on an existing scheme if the scheme experiences any major changes after approval, or revoke the approval of a scheme. Conditions might cover issues such as the type of cases or sectors where a scheme may operate, requirements for training, governance requirements, internal review and other matters.
- 7 **Agree** to establish, in addition to the principle-based approval criteria (ie accessibility, independence, fairness, accountability, efficiency and effectiveness), mandatory considerations that the Minister must have regard to in deciding whether to approve a scheme.
 - 7.1 The extent to which the scheme's governance arrangements ensure the independence and accountability of the scheme.
 - 7.2 Whether the scheme's rules provide for periodic review, and the type of review required (ie internal or independent).
 - 7.3 The competency of the directors and senior managers of the scheme.
 - 7.4 Whether the scheme has adopted procedures to ensure that it has adequate funding to enable it to operate effectively.
 - 7.5 The cost to consumers to lodge a complaint with the scheme.
 - 7.6 The extent to which the scheme's members cover a particular sector or sectors, however, each scheme will be free to set restrictions or qualifications on membership of the scheme to ensure that the scheme operates in an efficient and effective way.
 - 7.7 Whether the scheme has adopted a minimum jurisdiction covering complaints about breach of contract or statutory obligation, and breach of an industry code. Schemes will also be free to adopt a wider jurisdiction, covering complaints of general unfairness, if the scheme members so desire.
 - 7.8 Whether any proposed monetary limit on liability of scheme members is appropriate for the particular sector or type of business carried on by scheme members.
 - 7.9 Whether the scheme's rules provide that it is free to consider any information or make any inquiry as it sees fit and can have reference to what the scheme considers fair and reasonable in the circumstances, rather than strict adherence to legal rules.
 - 7.10 The scheme's obligations under its rules to engage in awareness, promotion and education.
 - 7.11 The scheme's obligations under its rules to report to stakeholders.

- 8 **Agree in principle** that in the event of no schemes meeting the approval criteria or if there is not full coverage of the financial industry by those schemes which are approved, the legislation will provide reserve powers under which the Minister may, by regulation, establish a dispute resolution scheme (the “reserve scheme”).
- 8.1 **Invite** the Minister of Commerce to report back to Cabinet by 31 July 2007 with a more detailed proposal covering the powers of the reserve scheme, calculation of a levy on members of the reserve scheme, and the process for establishment of the reserve scheme.
- 9 **Agree** that a scheme’s rules must provide that a decision of the scheme is binding (subject to a limited exception) on the member in relation to whom it is made, but do not preclude a consumer from rejecting the scheme’s decision and taking alternative court action against a financial provider.
- 9.1 **Agree** that a member’s limited right to appeal from a decision of a scheme will be similar to rights available under the Disputes Tribunal Act for appeals against an order of a Disputes Tribunal. That is, an appeal is only allowed on the grounds that the proceedings were carried out in an unfair manner.
- 10 **Agree** that government involvement will be limited to approving schemes (including periodic renewal), receiving periodic reports, and powers of inspection if necessary, rather than involvement in the day-to-day operation of a scheme. Re-approval is to be obtained by schemes at 10 year intervals. Periodic reporting is to be annual and set out basic information about the activities of the scheme (eg number and type of complaints considered, promotional activities undertaken, etc), as well as identifying any systemic issues which the scheme considers require attention by government.
- 11 **Note** that, to assist affected parties in complying with the new regime, the Ministry of Economic Development will produce educational material: for dispute resolution schemes to help them meet their obligations in order to obtain approval; for financial institutions, to inform them of their obligation to join a dispute resolution scheme; for consumers, to inform them of the availability of new dispute resolution and redress mechanisms.
- 12 **Note** that the Ministry of Economic Development and other relevant agencies are working on various initiatives to improve consumer financial capability.

- 13 **Invite** the Minister of Commerce to issue drafting instructions to Parliamentary Counsel Office to give effect to the decisions above.
 - 13.1 **Agree** to delegate decisions on minor issues that arise as part of the drafting process to the Minister of Commerce.

Hon Lianne Dalziel
Minister of Commerce

Hon Judith Tizard
Minister of Consumer Affairs

Regulatory Impact Statement

EXECUTIVE SUMMARY

There is currently a problem for some consumers in accessing appropriate dispute resolution and redress mechanisms in those parts of the financial sector where voluntary, simple dispute resolution mechanisms do not exist. Consumers experience problems because of lack of knowledge about where to go, and because of complicated and expensive dispute resolution processes that make it not worthwhile to pursue complaints.

Voluntary industry-based dispute resolution schemes currently cover most banks and insurance companies, as well as many managed funds. The main gaps in the financial sector where consumers do not have access to industry-based dispute resolution include finance companies, building societies, credit unions, financial advisers and some superannuation schemes. In these areas, consumers must use the court system to seek redress.

The proposal is to require that all financial providers join an industry-based dispute resolution scheme which has been approved by the Minister of Commerce.

This option will ensure that, as an alternative to the courts, consumers have access to simple, low cost dispute resolution. Industry responsibility for funding and operating the dispute resolution schemes will provide incentives for financial providers to maintain appropriate customer service standards and ensure customers are treated fairly and reasonably.

ADEQUACY STATEMENT

The Regulatory Impact Analysis Unit has reviewed the RIS and considers the RIS is adequate according to the adequacy criteria.

STATUS QUO AND PROBLEM

Under the status quo, there are two voluntary industry-based dispute resolution schemes, the Banking Ombudsman and Insurance & Savings Ombudsman. While these schemes work very well in providing a simple, low cost dispute resolution service, access to these schemes is only available for consumers who are customers of these schemes' member firms. Other consumers must use the court system for dispute resolution and to obtain redress.

Banks, managed funds and insurance companies make up a large proportion of the New Zealand financial sector. The majority of these financial institutions are members of one of the existing schemes. However, while these schemes are available to a large number of consumers, dispute resolution is not available to consumers in all parts of the financial sector. The main gaps in the financial sector where consumers do not have access to industry-based dispute resolution include finance companies, building societies, credit unions, financial advisers and some superannuation schemes. These sectors are more fragmented and lack the cohesion present in the banking and insurance sectors which facilitated the establishment of the voluntary schemes.

While the court system (including the Disputes Tribunal) generally works well for most types of consumer disputes, it does have some disadvantages in the case of financial services. For example, the time, cost and complexity of initiating court action may dissuade some consumers from standing up for their rights. The Disputes Tribunal addresses these issues of cost and complexity; however, the monetary limit of \$7,500 (or \$12,000 with the agreement of the parties) for Disputes Tribunal claims will exclude many financial disputes.

Although the existing schemes have the capacity to take on new members, it is not expected that they will further extend their coverage without regulatory intervention. Voluntary industry-based dispute resolution provides a competitive advantage for member firms by enhancing their reputation and promoting consumer confidence in those firms. It is expected that there would be reluctance from those firms which are currently members of a voluntary scheme to extend coverage of the scheme to other parts of the financial sector.

In August 2006, the Ministry of Economic Development released a discussion paper which noted results from the National Consumer Survey on Awareness and Experience of Consumer Legislation (conducted by National Research Bureau Ltd on behalf of the Ministry of Consumer Affairs, October 2005) which showed that, while the level of consumer problems with misleading or unfair treatment by financial providers is relatively low, consumers experience problems in seeking and obtaining redress. Common reasons given by consumers included “did not know who to complain to”, “did not think it would make a difference”, and “couldn’t be bothered”.

There are problems in relation to both consumer knowledge of, and ability to access, dispute resolution mechanisms. For example, the National Consumer Survey found that 30 per cent of respondents believed that there is a problem about taking a case to the Disputes Tribunal or about the way that the courts work. Common comments by respondents included “costs, direct or indirect may be involved”, “time frame to get heard would be too long”, “time and effort required would not be worth it for such small amounts”, “not knowing where to start or how to go about it, or how to contact them”, and “intimidating experience”.

Some submissions to the discussion expressed the view that there was not a problem in relation to consumers’ access to dispute resolution. For example, one submission noted that consumer decisions to borrow or invest are not made because of the existence, nature or form of dispute resolution or redress procedures; decisions are made for more positive reasons often in ignorance of the existence of such procedures.

On the other hand, low financial literacy means that New Zealand consumers have limited ability to properly compare competing options offered by financial providers. If consumers do not have access to effective redress if things go wrong, this means that there are limited incentives for financial providers to treat customers in a fair and reasonable manner.

On balance, submissions on the August 2006 discussion paper supported the view that there is sufficient evidence of a problem to warrant further government action to improve access to redress in order to promote consumer confidence in financial markets.

OBJECTIVES

A robust and efficient financial sector, where the public has a strong basis for being confident in the sector, is an essential prerequisite for a strong and dynamic economy. In the context of consumer dispute resolution and redress, three further policy objectives support the overarching aim of a robust and efficient financial sector:

- Promote consumer/investor confidence in financial markets. Consumer confidence relies on three elements:
 - Consumers' expectations of a transaction are met by suppliers;
 - Consumers and suppliers have confidence in market rules and institutions;
 - Consumers have effective access to redress;
- Reinforce market incentives, within a competitive environment, to encourage fair and reasonable behaviour by financial providers towards their customers;
- Maintain resilience and stability of financial markets.

ALTERNATIVE OPTIONS

Consumer education and information This option would address the problem by building capability of consumers to make informed choices so that consumers will avoid unsuitable products, thus reducing the number of disputes. This option is seen as a long-term solution, rather than achieving immediate improvements in consumer confidence. This option would not address problems which occur after a contract has been entered into, such as maladministration or financial providers not properly following their own policies, or misrepresentation by financial providers prior to the transaction taking place.

Note that the benefits of improved consumer education will not be evenly distributed across all consumers. Education and information will have a proportionately bigger benefit for those consumers who have better ability to make use of information in their financial decisions, as well as those consumers who have access to a wide range of options in choosing financial products or providers

This option would be difficult to implement, for example it would be difficult to compel firms to provide effective generic education, rather than product-specific information. The financial sector consists of a large number of providers offering a wide range of products. If the obligation to provide consumer education falls on industry, firms will have an incentive to focus their education/information efforts on information specific to the products they offer. This will not assist consumers in making choices between competing products and suppliers or whether a product meets their return and risk needs.

Enhanced civil remedies and specialist courts/tribunals This option would involve adopting simplified court procedures (for example, through a specialist Disputes Tribunal) to improve consumer access to courts to seek redress. While the court

system (including the Disputes Tribunal) generally works well for most types of consumer disputes, it does have some disadvantages in the case of financial services. Cost and complexity may dissuade some consumers from initiating court action. These disadvantages were identified by the Financial Intermediaries Task Force, and include: evidential difficulties, particularly where advice or recommendations are given orally, and the factual background is complex; difficulties in establishing and/or quantifying loss, particularly where other factors, such as market fluctuations, have contributed to loss; disputes often focus on a highly specialised area of knowledge; and limitation issues – it may take a significant amount of time for problems with financial advice and information to become evident, so that claims may fall outside limitation periods.

A specialist tribunal would allow the accumulation of specialist expertise, and allow for setting monetary limits appropriate for financial disputes. However, as it would still be part of the court system, a specialist tribunal would still face the same problems currently experienced by courts, such as evidential difficulties and time limitations.

The main disadvantage of this option is that it would not encourage industry commitment, particularly because it would not leverage off the goodwill of the existing industry-based dispute resolution schemes.

This option would involve significant costs to government in establishing a new branch of the Disputes Tribunal. It is expected that this would increase the number of consumers taking court action and, while there would be a drop in the number of District Court cases as these claims could be heard in the new tribunal, there is likely to be a net increase in the costs for government in operating the court system.

Under this option there would be no costs to industry in establishing the new tribunal. It is expected that simplifying consumer access to a dispute resolution mechanism will result in an increase in consumers seeking redress, and this will mean increased costs for industry in defending complaints.

There will be some benefits to consumers under this option as it will enable consumers to take disputes to the specialist Disputes Tribunal rather than the District Court regardless of the amount in dispute. This will make dispute resolution easier and probably increase the number of complaints made by consumers. This option would retain existing Disputes Tribunal processes, such as a \$50 filing fee.

Single industry-based dispute resolution scheme which all financial providers would be required to join. The main advantage of this option is that a single scheme may be cheaper to operate due to efficiencies of scale, producing advantages for both financial providers and consumers. This is particularly significant given the relatively small size of the New Zealand financial industry and number of consumer complaints.

A single dispute resolution scheme would create a level playing field in terms of regulatory treatment. This would provide coverage across all sectors of the financial industry. This option would also address unnecessary barriers to entry that may hinder access for some firms to membership of a dispute resolution scheme. However, a one-size-fits-all approach may lack specialization or be too blunt to effectively deal with varying industry practices

This scheme would require the greatest degree of government involvement. This could have implications for industry commitment to the success of the scheme, for example, if firms come to see themselves as “regulated entities” rather than “members”.

There are a wide range of types of financial providers, from small businesses through to large banks and insurance companies. It may be difficult to achieve industry cohesion or a common understanding of the rules to be followed. This suggests that this option would require a greater degree of government intervention than the other options.

PREFERRED OPTION

Multiple industry-based dispute resolution schemes. Membership of an approved dispute resolution scheme will be mandatory for all financial institutions that are required to be registered, and financial advisers, who provide products or services to consumers; however, they are free to join any scheme. This means that the dispute resolution requirements would apply to the following financial institutions:

- banks;
- friendly societies;
- credit unions;
- building societies;
- industrial and provident societies;
- finance companies;
- issuers of equity and debt securities;
- issuers of collective investment schemes;
- trustees supervising these issuers;
- insurers;
- platform and portfolio service providers and custodians.
- lending businesses;
- financial leasing businesses;
- money or value transfer services (eg money remittance);
- money and currency changers;

as well as financial advisers.

Further work will be undertaken on the definition of “consumer” in particular sectors, with a report back to Cabinet by 31 August 2007.

An approved dispute resolution scheme is one that has satisfied the Minister of Commerce (following consultation with the Minister of Consumer Affairs and Minister of Finance) that it meets criteria of accessibility, independence, fairness, accountability, efficiency and effectiveness. In deciding whether to approve a scheme, the Minister must give regard to some mandatory considerations relating to the governance of the scheme, periodic reviews, the scheme's funding, the cost to consumers, membership restrictions, the scheme's jurisdiction, limits on liability of scheme members, evidence and processes, awareness, promotion and education, and reporting to stakeholders.

Government involvement will be limited to approving schemes (including periodic renewal), receiving periodic reports, and powers of inspection if necessary, rather than involvement in the day-to-day operation of a scheme. Re-approval is to be obtained by schemes at 10 year intervals. Periodic reporting is to be annual and set out basic information about the activities of the scheme (eg number and type of complaints considered, promotional activities undertaken, etc), as well as identifying any systemic issues which the scheme considers require attention by government.

The scheme approval process will include appropriate checks and balances, including a requirement for the Minister of Commerce to be satisfied that the scheme has undertaken appropriate consultation, timeframe for decisions, method of notifying approval, and other matters.

The Minister may impose conditions on the approval of a scheme or on an existing scheme if the scheme experiences any major changes after approval, or revoke the approval of a scheme. Conditions might cover issues such as the type of cases or sectors where a scheme may operate, requirements for training, governance requirements, internal review and other matters.

Under this option, the dispute resolution system is fully funded by industry. By allowing the various sectors of the financial industry to establish their own schemes, this option provides for the greatest degree of industry involvement and commitment, as well as taking advantage of the skills needed to address a particular part of the financial sector.

This option also provides that, in the event of no schemes meeting the approval criteria or if there is not full coverage of the financial industry by those schemes which are approved, reserve powers will allow for a government-established scheme.

A decision of a scheme will be binding on the member in relation to whom it is made, but will not preclude a consumer from rejecting the scheme's decision and taking alternative court action against a financial provider.

Risks of not implementing the preferred option

If this option is not implemented, there will continue to be many consumers who are unable to access simplified dispute resolution mechanisms and must resort to the courts to seek redress. This runs the risk of not achieving the key objective of promoting investor/consumer confidence in financial markets. It also would not establish any mechanisms for reinforcing market incentives to encourage fair and reasonable behaviour by financial providers towards their customers. The absence of a comprehensive industry-based dispute resolution system would also hamper the ability for government to monitor and obtain the necessary information (for example,

information about levels of compliance with the law, increased complaints about a firm as an indicator of potential collapse) so as to maintain resilience and stability of financial markets.

Impacts on government

There would be costs to government in approving schemes and monitoring the dispute resolution system, however these are not anticipated to be large. The proposals in this paper will result in additional roles and functions for the Ministry of Economic Development in providing advice to the Minister on approval of dispute resolution schemes, as well as liaising with, and producing educational material for, dispute resolution schemes, industry participants and consumers. These costs are estimated at \$0.3m per annum for the first two years and \$0.1m per annum thereafter.

If a reserve scheme is necessary, there will be some costs for government in establishing the scheme. However, a levy would be imposed which would allow for full cost recovery from financial providers who become members of the reserve scheme. A report back to Cabinet on the details of the reserve scheme, including the power to set a levy, is due by 31 August 2007.

Impacts on industry

It is anticipated that financial providers would incur three types of costs:

- Costs for internal complaints handling
- Internal costs incurred in responding to complaints through the dispute resolution body
- Membership fees levied by the dispute resolution body – whether fees are levied on a “per case” basis or consist of a general membership levy.

Costs might be incurred if a dispute resolution scheme requires, as a condition of membership, that its members establish internal complaints handling procedures. Note that not all financial providers will incur these costs, as many will already have internal complaints handling processes in place. A study in the United Kingdom indicated that the cost of an internal complaints handling system ranged between GBP50 and GBP1700 per case, depending on the size of firm and the type and volume of business it does (Financial Ombudsman Service (UK), *Complaints handling arrangements: feedback statement on CP33 and draft rules*, May 2000, www.fsa.gov.uk/pubs/cp/cp49.pdf, page 51). The August 2006 discussion paper requested comments (on a confidential basis if requested) from financial providers, however no submissions addressing this point were received.

The proposal does not impose additional costs for firms' internal costs incurred in responding to complaints through the dispute resolution body. These costs would be incurred by the firm regardless of the form of dispute resolution. For example, the firm would face similar (or possibly higher) costs in defending an action in the courts or Disputes Tribunal. Firms may experience increased costs if, as expected, this proposal results in an increase in complaints from consumers who would otherwise have been reluctant to complain through the courts or Disputes Tribunal. Improving ease of

access to dispute resolution will undoubtedly increase the number of consumers seeking redress. This may be thought to also lead to an increase in frivolous or vexatious complaints, however the experience of existing schemes has generally been that these complaints can be weeded out quite easily.

The current Banking Ombudsman and Insurance & Savings Ombudsman schemes operate on annual budgets of approximately \$1.2m and \$1m respectively. They are funded through a combination of an annual levy on members (depending on the size of the firm) and a case levy for each complaint considered by the scheme. The funding formulas adopted by the existing New Zealand schemes, as well as similar schemes in other countries, vary quite widely and are designed to reflect the particular nature of each scheme's members. Note that a case levy does not always represent the true marginal cost of additional cases, but must be set at such a level that it does not affect the incentives facing members in their decisions to either settle or fight a complaint.

While it is difficult to quantify the expected costs and benefits of industry-based dispute resolution for financial providers, the fact that the banking, insurance and savings sectors have voluntarily established dispute resolution schemes suggests that those sectors have found the benefits outweigh the costs. Other sectors, such as financial advisers, have not voluntarily established such regimes; however, this may be because these sectors are more fragmented and difficult to reach industry-wide consensus than banking or insurance.

It is expected that the proposal would have benefits for financial providers through improved consumer/investor confidence in financial markets. This will promote more efficient markets and encourage greater participation by consumers in financial markets, with consequent benefits for financial providers.

As the proposal is broadly similar to the regulatory regime in Australia, this will make it easier for New Zealand firms to expand into Australia as they will be familiar with the compliance requirements they would need to meet in Australia. Alignment with Australian standards will also make it easier for dispute resolution schemes to build their capability, as they will be able to take advantage of experience from overseas.

Impacts on consumers

While the establishment of an industry-based dispute resolution mechanism would not impose any direct costs on consumers, it is likely that any additional costs to financial providers would be passed through to consumers.

Virtually all existing industry-based dispute resolution schemes are free of charge to consumers. Schemes also put very few formal obstacles in the way of consumers seeking to use their services. For example, most schemes allow consumers to make contact by telephone or through the internet.

The ease of access to current industry-based dispute resolution schemes can be contrasted with the court system, where consumers must pay a fee to lodge a claim. The official forms for lodging claims can also be confusing and intimidating for some consumers. This is especially beneficial for less educated consumers.

Access to industry-based dispute resolution will provide considerable benefits for consumers. For example, a free complaints service would enable consumers to obtain redress for small-value claims, as they would otherwise put up with the problem rather than commence court action. This is especially beneficial to low-income consumers. An informal dispute resolution style, in conjunction with an awareness-raising campaign, would be especially beneficial for less educated consumers. It is difficult to quantify the detriment currently suffered by consumers as a result of inability to access redress.

An increase in the number of consumer complaints would indicate an increasing degree of consumer sophistication. This has flow-on benefits for financial providers and the community in improving service standards in the industry. It may also flow through to more confident participation in financial markets by consumers, including, for example, encouraging saving.

Steps taken to minimise compliance costs

The existence of multiple dispute resolution schemes will allow firms to seek out the scheme which has the best fit. This will minimise costs for firms in complying with the scheme's rules.

The criteria for approval of a scheme have been designed with a principles-based approach so as to give schemes flexibility to meet the requirements in the best way for them, ie cheapest and most effective.

Impact on the stock of regulation

New legislation will be required to implement this proposal. This proposal links with the proposed new registration regime for financial institutions.

IMPLEMENTATION AND REVIEW

The proposal will be implemented with commencement in two stages. Stage 1, which establishes the rules for approval of dispute resolution schemes, will commence immediately following enactment of the legislation (and any regulations, if necessary). Stage 2, which will be the mandatory requirement for financial institutions to join an approved dispute resolution scheme, will come into force at the same time as the requirement to register in 2012.

To assist affected parties in complying with the new regime, the Ministry of Economic Development will produce educational material for dispute resolution schemes to help them meet their obligations in order to obtain approval; for financial institutions, to inform them of their obligation to join a dispute resolution scheme; for consumers, to inform them of the availability of new dispute resolution and redress mechanisms.

Compliance by firms with the requirement to join a dispute resolution scheme will be enforced by the proposed Registrar of Financial Service Providers through the registration regime (as outlined in the accompanying paper "Review of Financial Products and Providers: Registration of Financial Service Providers").

The effectiveness of the new dispute resolution regime in achieving its objectives will be monitored through the annual reports which approved dispute resolution schemes are required to submit to the Minister.

There is a risk that no dispute resolution schemes will seek or obtain approval, however this has been managed by consultation with industry and potential schemes. The level of support for industry-based dispute resolution shown through consultation on the discussion paper indicates that industry is committed to successfully implementing the proposal.

CONSULTATION

Stakeholder Consultation

The proposals were the subject of a discussion paper which was released in August 2006, along with other discussion papers in the Review of Financial Products and Providers. 139 submissions were received on the RFPP papers, of which 42 contained comments on consumer dispute resolution.

Some key concerns raised by submitters include:

- Some submissions related to the existence of a problem and the ability of improved dispute resolution arrangements to solve the problem (eg one submission noted that consumer decisions to borrow or invest are not made because of the existence, nature or form of dispute resolution or redress procedures; decisions are made for more positive reasons often in ignorance of the existence of such procedures) – this has been addressed by noting that dispute resolution is only one component of consumer confidence, and further work on improving consumer financial capability is also ongoing.
- Concerns were expressed that government intervention might damage the existing goodwill and industry commitment to external dispute resolution – this has been addressed by ensuring that the approval criteria for dispute resolution schemes closely reflect current practices as much as possible.
- Concerns were expressed that the proposal could result in industry funding the dispute resolution system but without any say in its operation – this has been addressed by limiting government involvement to approval of schemes, with a hands-off approach to the day-to-day governance and operation of dispute resolution schemes.
- Concerns were expressed about the potential scope of the proposed dispute resolution system – this has been addressed through limiting access to “consumers” (note that MED will be undertaking further work on establishing appropriate definitions of consumer in particular sectors), and through requiring that the Minister must have regard, when deciding whether to approve a scheme, to matters such as the jurisdiction of the scheme and any monetary limit on the liability of scheme members.

Government Departments/Agencies Consultation

The following government agencies have been consulted on the proposals in this paper: Ministry of Consumer Affairs, Reserve Bank, Treasury, Ministry of Justice, Securities Commission, Retirement Commission and Commerce Commission. No significant concerns have been raised.